

The 2002 Linkage Excellence in Management & Leadership Series

Strategy in the New Competitive Landscape

Featuring CK Prahalad



Dear Participant:

Welcome to the fourth program in Linkage's 2002 Excellence in Management and Leadership Series. The seminar series is designed to bring inspiring and influential business thinkers to your organization live via satellite, videoconference, and the Web.

Today's program, Strategy in the New Competitive Landscape, features CK Prahalad, Harvey C. Fruehauf Professor of Corporate Strategy and International Business at the University of Michigan Business School, and Chairman of the Board and co-founder of Praja, Inc., a pioneer company in interactive event experiences.

Specifically, this program will focus on:

- The contours of the new competitive environment
- The value creation process
- Creating new markets
- Efficiency and innovation - a prerequisite for effective competition
- Rapid learning curves and "forgetting" curves
- Leadership demands on managers

CK Prahalad is the co-author of more than ten articles in *Harvard Business Review*, three of which won the McKinsey Prize. His article, "The Core Competence of the Corporation" is the most reprinted HBR article ever. The book, *Competing for the Future*, co-authored with Gary Hamel, has been printed in thirteen languages and was considered the best business book of 1994.

These participant materials have been designed to complement your conversation with CK Prahalad. Use them to record your notes, ideas, questions, and insights. At specified points during the program, you will be asked to submit questions for Dr. Prahalad to address during the question-and-answer segment (scheduled toward the end of the program).

Learning is an activity that requires more than passively watching a speaker. Simply watching today's program will neither instill leadership knowledge or skills, nor result in an immediate change in your organization's culture and strategic positioning. Learning requires the active engagement of your mind and spirit - the motivation and drive to reflect, apply, practice, and experiment.

About Linkage

Linkage, Inc. is a leading provider of leadership and management development training programs, services, and products. More than 30,000 executives and management professionals have attended a Linkage institute, conference, workshop, or corporate education program. Linkage also provides assessment, consulting, and research services to Fortune 500 companies and other leading organizations. Founded in 1988, Linkage is headquartered in Lexington, Massachusetts, with regional offices located in Atlanta, Brussels, London, Minneapolis, and San Francisco. In both 1997 and 1998, Linkage was honored as one of the “Inc. 500 Fastest Growing Private Companies in the United States.”

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SECTION 1

Satellite Program Materials

What You Will Learn

Participation in this program with CK Prahalad is your opportunity to learn about the new view of strategy that focuses on value creation; the new competitive landscape influenced by deregulation, technological and industry convergence, and the Internet; and, creating new markets.

Question-and-Answer Session

- If you are participating only in the live presentation of this program, call in, fax, or e-mail your questions to CK Prahalad using the question sheet on page 15.
- If you are participating in a post-broadcast program, share your questions with your seminar coordinator and your colleagues during that time.

When the Session Has Concluded

- Your feedback is valuable in ensuring the integrity of future programs. We take pride in providing relevant, thought-provoking and enlightening programs - and we rely on you to help make this happen. Complete your participant evaluation form at: <http://www.linkageinc.com/surveys/research/eval0202.htm>
- To further reinforce your understanding of today's information, as well as hone other aspects of your leadership skills, complete the recommended Post-Presentation Activities that begin on page 13.

Pre-Presentation Activities

- Become familiar with CK Prahalad's accomplishments by reading the following biographical sketch:

Dr. Prahalad specializes in corporate strategy and the role and value added of top management in large, diversified, multinational corporations. Since completing his D.B.A. from Harvard University in 1975, he has been a visiting research fellow at Harvard, a professor at the Indian Institute of Management, and a visiting professor at the European Institute of Business Administration (INSEAD).

In addition to *Competing for the Future*, his books include *The Multinational Mission: Balancing Local Demands and Global Vision* (1987) with Yves Doz.

Professor Prahalad's contributions to strategic thinking are widely acknowledged.

In 1992, *Business Week* described him as a "brilliant teacher...Prahalad may well be the most influential thinker on corporate strategy today." He was named one of the top ten teachers in the world in *The Wall Street Journal's* Special Report on Executive Education (September 1993). In 1995, he received the American Society for Competitiveness Award for his outstanding academic contribution to competitiveness.

Dr. Prahalad has consulted with top management at a variety of firms including AT&T, Cargill, Citicorp, Colgate Palmolive, Honeywell, Oracle, Revlon, TRW, and Unilever.

- Read the following excerpt of an article co-authored by the presenter:

***Co-Opting Customer Competence* by CK Prahalad and Venkatram Ramaswamy**
(Harvard Business Review, January-February 2000)

Overview

Business competition used to be a lot like traditional theater: On stage, the actors had clearly defined roles, and the customers paid for their tickets, sat back, and watched passively. In business, companies, distributors, and suppliers understood and adhered to their well-defined roles in a corporate relationship. Now the scene has changed, and business competition seems more like the experimental theater of the 1960's and 1970's - everyone and anyone can be part of the action.

Thanks largely to the Internet, consumers have been increasingly engaging themselves in an active and explicit dialogue with manufacturers of products and services. What's more, that dialogue is no longer being controlled by corporations. Individual consumers can address and learn about businesses either on their own or through the collective knowledge of other customers. Consumers can now initiate the dialogue; they have moved out of the audience and onto the stage.

Customers are fundamentally changing the dynamics of the marketplace. The distinguishing feature of this new marketplace is that consumers become a new source of competence for the corporation. The competence that customers bring is a function of the knowledge and skills they possess, their willingness to learn and experiment, and their ability to engage in an active dialogue.

The unit of strategic analysis has moved from the single company, to a family of businesses, and finally to what people call the "extended enterprise," which consists of a central firm supported by a constellation of suppliers. But the recognition that consumers are a source of competence forces managers to cast an even wider net. Competence now is a function of the collective knowledge available to the whole system - an enhanced network of traditional suppliers, manufacturers, partners, investors, and customers.

The Evolution and Transformation of Customers

Customers are stepping out of their traditional roles to become cocreators as well as consumers of value. This table maps their evolution through three stages and along several key dimensions.

	Customer as a Passive Audience			Customers as Active Players
	Persuading predetermined groups of buyers	Transacting with individual buyers	Lifetime bonds with individual customers	Customers as cocreators of value
Time frame	1970s, early 1980s	Late 1980s and early 1990s	1990s	Beyond 2000
Nature of business exchange and role of customer	Customers are seen as passive buyers with a predetermined role of consumption.			Customers are part of the enhanced network; they cocreate and extract business value. They are collaborators, codevelopers, and competitors.
Managerial mind-set	The customer is an average statistic; groups of buyers are predetermined by the company.	The customer is an individual statistic in a transaction.	The customer is a person; cultivate trust and relationships.	The customer is not only an individual but also part of an emergent social and cultural fabric.
Company's interaction with customers, and development of products and services	Traditional market research and inquiries; products and services are created without much feedback.	Shift from selling to helping customers via desks, call centers, and customer service programs; identify problems from customers, then redesign products and services based on that feedback.	Providing for customers through observation of users; identify solutions from lead users, and reconfigure products and services based on deep understanding of customers.	Customers are codevelopers of personalized experiences. Companies and lead customers have joint roles in education, shaping expectations, and cocreating market acceptance for products and services.
Purpose and flow of communication	Gain access to and target predetermined groups of buyers. One-way communication.	Database marketing; two-way communication.	Relationship marketing; two-way communication and access.	Active dialogue with customers to shape expectations and create buzz. Multilevel access and communication.

Customers as a Source of Competence

Some industries have already gone further than others in drawing on the competencies of customers. For example:

- More than 650,000 customers tested a beta version of Microsoft's Windows 2000 and shared their ideas for changing some of the product's features. The value of the collective R&D investment by Microsoft's customers in co-developing Windows was estimated at more than \$500 million worth of time, effort, and fees.
- Cisco gives its customers open access to its information, resources, and systems through an on-line service that enables them to engage in a dialogue.

Harnessing the competencies of the consumer is not an easy task. At a minimum, managers must come to grips with four fundamental realities in harnessing customer competence:

1. *Encouraging Active Dialogue*

- It is critical for companies to understand the purpose, meaning, and quality of the dialogue from the customer's perspective.
- A dialogue must evolve - or die. Companies are going to have to find ways to process what they learn from customers so they can bring the dialogue forward and keep the consumer's interest.
- Progressive Internet companies have adapted best to the new dialogue. For example, each time an Amazon.com customer accesses the company's Web site, the on-line bookseller provides recommendations based not only on the customer's previous purchases but also on the purchases of other people who have bought similar books. As its customers' tastes and preferences evolve, Amazon's engagement with them reflects those changes.

2. *Mobilizing Customer Communities*

- Thanks to the Internet, customers in the new economy are finding it easier to form, on their own, self-selecting virtual communities.
- The power of such communities derives in large measure from the speed with which they can be mobilized - this is already transforming the management of brands.

3. *Managing Customer Diversity*

- As companies embrace the market as a forum, they become more vulnerable to customer diversity. This is particularly true of companies that sell technology intensive products, which are sensitive to variations in customers' sophistication.
- Consumer concerns about privacy and security can also accentuate the diversity among users.
- Apart from technology, globalization in the marketplace also heightens variation in customer sophistication. For example, Lucent Technologies has to contend with battalions of new and unknown customers, many of whom have limited or no knowledge of the telecom business. The only common denominator among them is a desire to participate in the telecommunications revolution.

4. *Co-creating Personalized Experiences*

- The customer is no longer interested in buying a product. The product, in fact, is no more than an artifact around which customers have experiences.
- It is important to distinguish personalization from customization:
 - Customization assumes that the manufacturer will design a product

to suit a customer's needs. For example, a customer of an on-line florist *customizes* flowers by choosing from a menu of features.

- Personalization is about the customer becoming a co-creator of the content of their experiences. In contrast, this same customer *specifies and designs* the type, quantity, and arrangement of flowers, vases, and colors they desire (vs. choosing from a menu of services).

The Shifting Locus of Core Competencies

	The company	Family/network of companies	Enhanced network
Unit of analysis	The company	The extended enterprise—the company, its suppliers, and its partners	The whole system—the company, its suppliers, its partners, and its customers
Resources	What is available within the company	Access to other companies' competencies and investments	Access to other companies' competencies and investments, as well as customers' competencies and investments of time and effort
Basis for access to competence	Internal company-specific processes	Privileged access to companies within the network	Infrastructure for active ongoing dialogue with diverse customers
Value added of managers	Nurture and build competencies	Manage collaborative partnerships	Harness customer competence, manage personalized experiences, and shape customer expectations
Value creation	Autonomous	Collaborate with partner companies	Collaborate with partner companies and with active customers
Sources of managerial tension	Business-unit autonomy versus leveraging core competencies	Partner is both collaborator and competitor for value	Customer is both collaborator and competitor for value

Managing the Personalized Experience

To provide personalized experiences, companies must create opportunities for customers to experiment with and then decide on the level of involvement they want in creating a given experience. Since the level of customer engagement cannot be predetermined, companies will have to give consumers as much choice and flexibility as possible - in the channels of distribution and communication and in the design of products.

- *Managing Multiple Channels of Experiences*
 - The Web is an incredibly rich channel for direct dialogue. It has also spawned more efficient business models. For example, a bank saves 80% of its costs when customers transact business using a PC; the customer also saves time and travel costs.
 - But, research shows that a consumer's experience with a company is

highly influenced by the environment in which it occurs. For example, Wells Fargo tried to force its customers to use PC-based banking services, without much success.

- The method by which customers and companies communicate is an integral part of creating an experience. The more environments a company can provide, the richer its customers' experiences are likely to be. For example, the Borders Books Web site and the layout of its bricks-and-mortar stores and cafes reinforce each other.
- Most companies will find that they have to manage and integrate several distributions channels - facing three key challenges:
 - Ensuring that the nature and quality of the fulfillment - the personalized experience for the individual - is not very different across channels
 - Developing the infrastructures needed to support a multi-channel distribution network (e.g., information technologies, billing system)
 - Combining telecommunications and Internet infrastructure with a physical logistics and service infrastructure.
- It is no longer about e-commerce, but f-commerce - the fulfillment of goods and services that can't be downloaded. For example, Webvan Group, a fast-growing on-line grocery merchant, placed a \$1 billion order for the Bechtel group to build highly automated warehouses in 26 markets across the United States.
- *Managing Variety and Evolution*
 - Customers judge a company's products not by their features but by the degree to which a product or a service gives them the experiences they want. For example, the driver of a luxury car equipped with a navigation system might want to use the system only to get a map and check the number of miles to his destination. However many capabilities the navigation system has, that driver will judge the system's performance according to the ease with which he can do those things.
 - Managing the variety of customer experiences is not the same as managing variety in products. It is about managing the interface between a company and its customers; the range of experience transcends the company's products.
 - Managers must develop a product that shapes itself to users' needs, not the other way around. - and, the product has to evolve in a way that enables future modifications and extensions based both on customers' changing needs and on the company's changing capabilities.
 - For example, consider the incorporation of TV features into PC-processor-powered products vs. embedded processors (microchips) vs. embedded intelligence (e.g., children's educational software from the Learning Company or TiVo, a home entertainment product from Philips).

- *Shaping Customers' Expectations*
 - Harnessing customer competence and managing personalized experiences requires cooperation from consumers. They must be sensitive to "what is next" - and that means companies must shape their expectations.
 - Shaping expectations is about engaging current and potential consumers in public debate. It is about educating customers and being educated - educated customers can be advocates and activists for the company.

Customers as Competitors

Armed with knowledge, customers are much more willing to negotiate terms and prices with companies. And, it's not just the way that consumers judge and negotiate the price for a product that's changing - it's the price-setting mechanism itself.

- The popularity of businesses such as eBay and Priceline.com suggests that the auction is increasingly serving as the basis for pricing goods and service on-line.
- From the customer's perspective, the advantage of the auction process is that prices truly reflect the utility to that customer, at a point in time, of the goods and services being purchased. In other words, the customer pays according to her needs rather than according to the company's need.
- Managers everywhere will have to get used to the idea that they are price takers as well as price makers. As customers become more knowledgeable and recognize that they have choices and the power to negotiate, more businesses will feel pressure to adopt an implicit (if not an explicit) auction process.

Preparing the Organization

Readying the organization for customer competence in the new economy will require a major overhaul of the company's traditional governance systems and organizational structures.

- Accounting standards need to factor in intellectual and human capital - a capital investment vs. treating training as an expense. The competence of customers is also an intangible asset - it should be considered capital.
- A project management approach needs to be adopted to evaluate the performance of people and businesses vs. reliance on quarterly and annual budget reviews.
- Systems that cater to the constant reconfiguration of the supply chain as a result of the existence of multiple distribution channels are needed.

There are also a host of implications for leaders and managers:

- Organizational flexibility is critical - create "Velcro" organizations in which resources can be reconfigured seamlessly and with as little effort as possible.
- Be prepared to deal with the psychological and emotional traumas of employees, as a result of pushing the frontier of business practices.
- Build the essential skills of collaboration, negotiation, learning, teaching, transferring knowledge across boundaries, and attracting - and retaining - people who are self-motivated to change.
- Maintain a stable center by providing emotional anchors - a strong set of organizational values.
- Provide leadership that is intellectually vigorous and administratively savvy.
- Hone your ability to amplify weak signals, interpret their consequences, and reconfigure resources faster than competitors.

During this Program

- Participate!
- Submit questions to be addressed by CK Prahalad during the question-and-answer session. Dr. Prahalad will respond to questions in the latter third of the program. To submit questions, either complete the fax form found on page 15, or call in or send an e-mail when prompted during the program.
- Use the following Participant Materials to follow along with the presentation. Take notes below the slides on the following pages.

Post-Presentation Activities

- Complete and submit the participant evaluation form - found at: <http://www.linkageinc.com/surveys/research/eval0202.htm>
- Review the key points and your notes and insights to reinforce your learning.
- Read books and articles co-authored by CK Prahalad:

The Boundaryless Organization: Breaking the Chains of Organizational Structure, Jossey Bass, 1995.

Competing for the Future, Harvard Business School Press, 1996.

"The Co-Creation Connection," *Strategy and Business*, Second Quarter, 2002.

"The Core Competence of the Corporation," *Harvard Business Review*, April 2001.

"Corporate Imagination and Expeditionary Marketing," *Harvard Business Review*, July 1991.

"Strategic Intent," *Harvard Business Review*, May 1989.

SECTION 2

Forms

Question Sheet

Use this form to write your question for CK Prahalad or for discussion among your colleagues. Please write clearly.

Name (optional)

Organization

Location

Your question (25 words or fewer):

Tel 1-800-489-8814 (from within U.S.)
 801-303-7412 (from outside U.S.)

Fax 1-877-892-0170 (from within U.S.)
 646-349-3661 (from outside U.S.)

Email leadership2002@linkage-inc.com